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No. 94-695

IN THE

Supreme Court of the United States

October Term, 1994

INTERNATIONAL BUSINESS MACHINES CORPORATION,

Petitioner,

v.

ALLEN-MYLAND, INC.,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

REPLY BRIEF OF PETITIONER

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REPLY BRIEF OF PETITIONER

Rather than address the merits of the Petition ("Pet."), Respondent Allen-Myland, Inc. ("AMI") seeks in its brief in opposition ("Opp.") to evade review of the Third Circuit's decision by reinterpreting it. Thus, AMI essentially argues that the questions on which Petitioner International Business Machines Corporation ("IBM") seeks review were all answered in IBM's favor by the Court of Appeals. In doing so, AMI apparently concedes that: (1) there should be a business justification defense to claims of per se tying (Opp. 18); (2) used equipment can only be excluded from a market if it is established as a matter of fact that new equipment and used equipment do not effectively compete with each other (Opp. 21); and (3) Rule 52 review by a Court of Appeals should be based on the entire record presented to the District Court (Opp. 23-24).

IBM is, of course, willing to accept those concessions should there be a remand to the District Court in this case. But

the important point here is that if the Third Circuit had really done what AMI says it did, there would be nothing to remand. The Court of Appeals would have affirmed the District Court's judgment because: (1) as the District Court held (and AMI never appealed), there were procompetitive business justifications for IBM's actions; (2) there was no evidence of IBM having controlled the competition that was undisputed to exist between new and used equipment; and (3) the Third Circuit plainly did not review the entire record that the District Court saw and heard while trying this case.

But whatever line AMI is currently attempting to walk in this litigation, unless the Third Circuit's opinion is reviewed and reversed by this Court, it will stand as precedent for a subversion of the policies of the antitrust laws, in conflict with the decisions of this Court and other Circuits. The important legal questions raised by the Third Circuit's opinion—which AMI now apparently agrees should be resolved in IBM's favor—ought, therefore, to be settled definitively by this Court.

I. UNLESS REVERSED, THE THIRD CIRCUIT'S OPINION WILL STAND AS PRECEDENT FOR THE POSSIBLE PER SE ILLEGALITY OF PROCOMPETITIVE ACTIVITIES.

The decision of the Third Circuit places squarely before this Court the first question presented by the Petition—whether a procompetitive business practice can be an illegal per se tie-in. AMI does not dispute the broad importance of that question.[1]

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[1] AMI's bald assertion (Opp. 19 n.20) that there is no split in the Circuits on this point is wrong. As demonstrated in the Petition (Pet. 16), and as further demonstrated below, the Third Circuit's decision here conflicts with decisions in the First, Fourth, Seventh and Ninth Circuits. A similar conflict between those Circuits and the Second and Sixth Circuits is plain from the cases discussed in the Petition (Pet. 15), AMI's halfhearted suggestion to the contrary (Opp. 19 n.20) notwithstanding. Moreover, AMI ignores the fundamental point that the Third Circuit's decision and decisions in the Second and Sixth Circuits all conflict with this Court's decisions. *See* Pet. 12-13. In addition, as noted in the Petition (Pet. 17 n.10), the general uncertainty on this important issue has been recognized by commentators.

Rather, AMI contends that the Court of Appeals' decision does not adequately put the question before this Court because the issues involved have not yet been resolved by the lower courts in this matter. Opp. 15-16, 18. That is wrong. All questions of business justification have been fully and finally determined in IBM's favor.

AMI contended before the District Court that IBM's alleged tying practices were illegal under both per se and rule of reason standards. The District Court found for IBM on both. In particular, as the Court of Appeals held, quite separately from the market power and foreclosure issues under the per se analysis, "[t]he [district] court also found that net pricing did not violate section 1 under a rule of reason analysis *because sufficient procompetitive reasons existed for it.*" A5 (emphasis added). And, as the Court of Appeals expressly noted: "The district court's decision under the rule of reason has not been appealed." A5 n.6. It is well established in the Third Circuit that issues not raised on appeal are waived. *See, e.g., Nagle v. Alspach*, 8 F.3d 141, 143 (3d Cir. 1993), *cert. denied*, 114 S. Ct. 1337 (1994); *Jackson v. University of Pittsburgh*, 826 F.2d 230, 237 (3d Cir. 1987), *cert. denied*, 484 U.S. 1020 (1988). The Court of Appeals necessarily did not review the District Court's findings with respect to the "procompetitive reasons" for IBM's actions.

Thus, the Third Circuit's decision to reverse and remand on the per se analysis was made despite the District Court's acceptance (not appealed by AMI) of IBM's business justifications. As the District Court found, the effect on the 308X program of eliminating IBM's net pricing policy would have been "devastating" (A89)—*i.e.*, without net pricing the massive increase in cost of producing the 308X's underlying TCM technology would have prevented its introduction. Thus, the District Court found that "[n]et pricing facilitated the

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See, e.g., David E. Lazaroff, *Reflections on Eastman Kodak Co. v. Image Technical Services, Inc.: Continued Confusion Regarding Tying Arrangements and Antitrust Jurisprudence*, 69 Wash. L. Rev. 101, 143-44 (1994).

development and marketing of TCM technology, and *thereby enhanced technological progress and economic competition in the data processing industry*." A90 (emphasis added). AMI never sought to overturn those findings on appeal. As IBM demonstrated in the Petition (Pet. 11-18), had the Third Circuit accepted the existence of the business justification defense, then there should have been no remand: IBM's activities, which allowed for the creation not only of a new product line but of a whole new, more modular technology, should have been protected.

In an attempt to avoid this conclusion, AMI contends that, in fact, the Court of Appeals "vacated the judgment for IBM on the tying count of AMI's complaint in its entirety, not just on the *per se* theory of liability." Opp. 18. That is simply wrong. As the procedural history of this case makes plain, AMI did not appeal the District Court's decision in favor of IBM on the rule of reason theory of liability. The Third Circuit did not—and could not—vacate a decision on an issue that (1) was not appealed; (2) the Court of Appeals did not believe to be before it; and (3) Third Circuit law treats as a waived issue.

In addition to rewriting the procedural history of this case, AMI makes the analytically erroneous claim that when the Court of Appeals vacated the District Court's market definition and finding of lack of market power, it somehow rejected the District Court's business justification findings as well. Opp. 17-18. This is, again, a transparent effort to suggest that IBM's first question is not properly before this Court, but the analytical flaw is plain: business justifications under the rule of reason become operative precisely when the requisite evidence of a tie-in *is* found to exist. And, again, AMI did not challenge on appeal the District Court's business justification analysis. Having made that choice, AMI's effort to treat the issue as if it had been challenged and vacated by the Court of Appeals (and may now be reconsidered by the District Court on remand (Opp. 18)) is untenable.[2]

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[2] AMI's additional argument (Opp. 17) that IBM did not adequately raise this issue below is simply untrue, as is clear from AMI's own brief. As

The essence of AMI's argument appears to be that because the harm to AMI is now again an open factual issue, the procompetitive effects of IBM's actions can be overridden (or at a minimum reassessed). But those procompetitive effects have been conclusively determined to exist, and to override them would be to permit the antitrust laws to be used as a sword to stifle competition instead of a shield to protect it. It is flatly contrary to this Court's well known admonition that "[t]he antitrust laws . . . were enacted for 'the protection of competition not competitors.'" *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977).

II. UNLESS REVERSED, THE THIRD CIRCUIT'S OPINION WILL STAND AS PRECEDENT FOR EXCLUDING FROM MARKETS, AS A MATTER OF LAW, USED PRODUCTS MADE BY THE DEFENDANT BUT MARKETED BY OTHERS.

There is no dispute that the question of market definition should be one of fact, not of law. *See Eastman Kodak Co. v. Image Technical Servs., Inc.*, 112 S. Ct. 2072, 2082 (1992) ("*Kodak*"). The dispute here is whether the Court of Appeals ruled as a matter of law that used IBM equipment did not compete with, and was not in the same market as, new IBM equipment. AMI contends that the Court of Appeals held that this was a factual question, that the District Court's

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AMI acknowledges (Opp. 17 n.17), IBM first pointed out to the District Court that business justifications are relevant to the per se analysis. Next, as AMI again acknowledges (Opp. 18 n.19), IBM pointed out to the Court of Appeals that, as the cases then stood, it would be unprecedented to ignore the "compelling business justifications" for IBM's actions and to condemn it as per se illegal. Brief for Appellee at 17-18. The language quoted by AMI from IBM's brief to the Third Circuit (Opp. 17) pointed out that, by narrowly construing the per se rule and not appealing the rule of reason decision, AMI was hoping to avoid consideration of IBM's business justifications. IBM specifically brought to the Third Circuit's attention the issue that IBM raises again here and which AMI seeks to avoid: that the law should not condemn as per se illegal an activity that is procompetitive, and certainly not when that activity has been finally adjudicated to be procompetitive. Brief for Appellee at 18.

consideration of used equipment was clearly erroneous, and that it should be reconsidered on remand. If the Court of Appeals ruled on this issue as a matter of law, then AMI apparently does not challenge (Opp. 20-21) IBM's position (Pet. 18-24) that a conflict has been created with the law of this Court and in other Circuits, and that this is a certworthy issue.

AMI's interpretation of the Third Circuit's opinion cannot withstand scrutiny. In reaching its conclusion, the Court of Appeals did not even purport to reverse the District Court's inclusion of used IBM equipment in the market definition under the clearly erroneous standard, nor did it remand for further consideration of this issue. Rather, the Court of Appeals stated flatly that the District Court had "erred"; on remand, the District Court was not asked to reconsider anything—it was directed to "include only leases of used, non-IBM mainframes and determine the extent to which those leases reduce IBM's market share." A11, A12. Whatever AMI is now willing to argue in order to try to avoid a writ of certiorari, the Third Circuit's determination will necessarily be read as what it is—a *legal* determination.[3]

It is plain that the Court of Appeals based its decision on this point on *United States v. Aluminum Co. of Am.*, 148 F.2d 416 (2d Cir. 1945) ("*Alcoa*"), to which it expressly gave "weight as precedent". A10 n.10. Even AMI has not claimed that the market for aluminum ingot in the 1940s is in any way a factual "precedent" for the market for computer equipment in the 1980s, and the Court of Appeals' decision can only sensibly be read to be deriving a rule of law from the *Alcoa* decision.

Two additional features of the Court of Appeals' decision confirm the nature of what the court did. *First*, the only thing approaching evidence to which the court referred in this context

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[3] Indeed, the Third Circuit's decision to exclude used IBM equipment was made in the face of abundant evidence, cited at length in the petition (Pet. 20 n.12), that new and used IBM equipment competed against each other, and an *amicus* brief on behalf of leasing companies of used equipment that confirmed the competitive constraint that used equipment places on IBM (Pet. 19 n.11).

was the notion that IBM "enhanced" its control by taking possession of those TCMs removed as a result of net priced upgrades. A11; Opp. 20. Only *some* 308X upgrades were net priced, and only *some* 308X computers were upgraded with net priced upgrades in connection with particular transactions. A40-41, A58. Yet, the Court of Appeals held that *all* used IBM-manufactured computers must be excluded from the relevant market. A11-A12. Surely, IBM's purported "control" over removed TCMs from some 308X upgrades cannot form the basis for excluding all used 303X IBM computers,[4] or all used 308X computers that were not the subject of net priced upgrades. But the Court of Appeals nevertheless excluded them. There is no way that the court's limited factual discussion could yield its sweeping result.

Second, the Court of Appeals' limited discussion of the facts is cast in terms of "enhanc[ing]" IBM's control and "further reduc[ing]" the leasing companies' ability to compete. A11 & n.11; Opp. 20-21. On its face, the discussion presumes the existence of control wholly apart from this factual context. And that is not surprising, since the court devotes the majority of the analysis in its opinion to the precedential rule of *Alcoa*.

In sum, AMI's interpretation to the contrary notwithstanding, the Court of Appeals broadly excluded used IBM equipment from the market on the basis of the *Alcoa* case. That ruling was—and could only have been—a matter of law.

In addition, as IBM pointed out in the Petition (Pet. 22-24), even if the Court of Appeals' decision is somehow regarded as a factual determination based on an economic theory—and thus one that the District Court is free to reconsider—the underlying economic theory being employed has long been regarded as unsound. Not only have commentators rejected it (Pet. 22-23), but no court has ever applied it so as to ignore the actual competitive impact of used equipment, as the Third Circuit did

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[4] The 303X line of computers immediately preceded the 308X line (A2-A3), and used 303Xs were sold and leased in competition with 308Xs.

here.[5] Indeed, the *Alcoa* theory was narrowly limited to the peculiar facts before the Second Circuit by the District Court on remand in that very case, *see* 91 F. Supp. 333, 357 (1950), and by this Court in *United States v. E. I. DuPont de Nemours & Co.*, 351 U.S. 377, 396 n.23 (1956). Where, as here, a defendant is not effectively the sole manufacturer of equipment, then the *Alcoa* theory has been held not to apply. *See* Pet. 23-24. AMI in no way challenges IBM's argument on this point and yet still seeks to avoid the writ of certiorari. There is no basis for doing so.

III. UNLESS REVERSED, THE THIRD CIRCUIT'S OPINION WILL STAND AS PRECEDENT FOR A COURT OF APPEALS ENGAGING IN ITS OWN FACTFINDING IN DISREGARD OF THE RECORD AND OF THE CREDIBILITY DETERMINATIONS OF THE DISTRICT COURT.

AMI makes three arguments in an effort to escape the writ of certiorari on the question of the proper application of Rule 52. None of those arguments has merit.

First, AMI argues that because the Court of Appeals *said* it was reversing on a clearly erroneous standard, its decision should not be reviewed by this Court. Opp. 22 & n.25. It can never be enough, however, merely to mouth a standard and not to apply it. It is for that reason that IBM has asked this Court expressly to set forth the three principles IBM recommends in

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[5] AMI quotes from *In re IBM Peripheral EDP Device Antitrust Litigation*, 481 F. Supp. 965, 980 (N.D. Cal. 1979), *aff'd*, 698 F.2d 1377 (9th Cir.), *cert. denied*, 464 U.S. 955 (1983), in an attempt to justify the Third Circuit's reasoning. AMI ignores what actually happened in that case (where the claims against IBM were all dismissed). It is true that the court excluded used equipment sold by third parties from the market definition, but at the same time it recognized that "the constraints these companies provide decrease the likelihood that defendant's market share reflects monopoly power." *Id.* at 979. That is, as the District Court here recognized (A52), the court there expressly took into account the effect on IBM's alleged market power of the competition from IBM-manufactured used products. That is precisely what the Third Circuit refused to do here.

the Petition (Pet. 25-26), and thus have Courts of Appeals properly address the evidence presented to, and relied upon by, the District Courts.[6] It is only in this way that litigants such as IBM can know—even if they disagree with the conclusions of a Court of Appeals—that the evidence they presented below was considered.

Second, AMI argues (Opp. 22) that "Rule 52(a) does not restrict the appellate court's corrective authority" in matters involving market definition. While Rule 52 is no limitation in cases involving legal issues, it is absolutely determinative of the standard to be used in reviewing factual issues, and, as this Court made plain in *Kodak*, market definition is always a factual issue. The cases cited by AMI (Opp. 22 & n.26) are entirely consistent. Thus, for example, in the principal authority cited by AMI—*United States v. Continental Can Co.*, 378 U.S. 441, 452 (1964)—and in the very language quoted by AMI, this Court reversed because the District Court applied the incorrect legal standard under Section 7 of the Clayton Act in "judging the facts". Here, where the sole question is whether the factual conclusions reached were supported by the record, Rule 52 necessarily controls.

Third, AMI argues that it was not error for the Court of Appeals to reverse the District Court's determination that the testimony of Larry Allen, AMI's President, was not credible and could not be relied upon, despite the extreme deference to be accorded to credibility determinations. Opp. 23. In support of that argument, AMI cites *Anderson v. City of Bessemer City*, 470 U.S. 564, 575 (1985), where this Court held that a determination that a witness's testimony *was* credible could be overturned on appeal if that determination was contradicted by

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[6] It is equally not enough for AMI simply to assert in its brief to this Court (Opp. 23-24) that the Court of Appeals did review all the evidence in the record. The Court of Appeals did not say that itself. Indeed, as IBM demonstrated in the Petition (Pet. 27-30), the Court of Appeals did not even discuss all the evidence cited by the District Court in support of its conclusions—let alone all of the record evidence—and nonetheless held the District Court's conclusions to be clearly erroneous.

documents or other objective evidence. This Court did not hold, however, that when a District Court has determined—however politely it couched that determination—that a witness was not to be believed (*see* A70), the witness's credibility could somehow be resurrected by the Court of Appeals. Nor would such a holding make sense where, as here, there was an absence of any other evidence to support the incredible testimony rejected below, and there was additional evidence (not addressed by the Court of Appeals) for regarding that testimony as untrue. Pet. 28-29. We submit that the Court of Appeals here failed to adhere to the requirements of Rule 52.

CONCLUSION

For the foregoing reasons, and for the reasons stated in the Petition, the Petition for writ of certiorari should be granted.

November 23, 1994

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